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No. 92-545

In The
Supreme Court of the United States
October Term, 1992

UNITED STATES OF AMERICA,
Petitioner

v.

GRANITE CONSTRUCTION COMPANY,
Respondent

On Petition for a Writ of Certiorari
to the United States Court of Appeals
for the Federal Circuit

BRIEF FOR GRANITE CONSTRUCTION COMPANY IN OPPOSITION

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QUESTION PRESENTED

The courts and contract appeals boards have long held that owners, both public and private, have the right to demand strict compliance with the specifications for a construction project. These tribunals, however, have uniformly recognized an exception to the right to strict compliance where the nonconforming work or product installed in the construction project meets or exceeds the owner's needs, and the cost of removal and replacement is so out of proportion to the resulting benefit as to amount to economic waste. Under these circumstances the owner may not require complete removal and replacement, but instead receives a price reduction for the diminution in value.

The question in this case is whether the Federal Circuit properly applied the "economic waste" principle to a federal construction contract so as to relieve a contractor of liability for the disproportionate cost of replacing installed nonconforming material that met or exceeded the government's needs.

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BRIEF FOR GRANITE CONSTRUCTION COMPANY IN OPPOSITION

STATEMENT

During construction of a lock and dam for the Corps of Engineers ("Corps"), it was discovered that respondent, Granite Construction Company[1] ("Granite"), had mistakenly installed waterstop in the concrete that did not conform exactly to the contract

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[1] Granite Construction Company is the party in interest in this case. Granite has no parent company and no subsidiaries that are not wholly owned.

specifications. Nevertheless, the embedded waterstop exceeded the project design safety factors some twenty fold and could withstand forty times the water pressure that would exist at the project. The nonconforming waterstop was, therefore, far stronger than the project required. The contracting officer directed that all nonconforming waterstop be chipped out of the concrete and replaced regardless of cost. The government refused to give any consideration to the adequacy of this waterstop or make a technical evaluation of the need to remove and replace the waterstop. Refusing even to consider repair of the existing installation, the Corps demanded "strict compliance" with the waterstop specification. The replacement was very costly, and Granite submitted a claim to recover its costs. The United States Court of Appeals for the Federal Circuit determined that the Corps acted arbitrarily and capriciously. It adopted the longstanding concept of economic waste and found that the Corps' directive to remove and replace the waterstop resulted in economic waste for which the government was liable.

1. This case involves a lock and dam project near Aberdeen, Mississippi constructed by Granite under a contract with the Corps of Engineers. The concrete lock was constructed in blocks ("monoliths") which were 30 feet wide, 42 feet long, and 60 feet high. Granite was required to embed a polyvinyl chloride waterstop in the vertical joint between the concrete monoliths in order to prevent water leakage through the joints. (Pet. App. 2a). The specified waterstop was not designed specifically for this project. Rather, the Corps used a uniform specification that had been developed for use on all Corps projects. It was designed

for use under much more severe conditions than would be encountered at the Aberdeen Lock and Dam. (Pet. 20-21, Pet. App. 63a-64a, 78a).

Granite purchased all the waterstop for the project from Vimco Concrete Accessories ("Vimco") for $5,752.80. Vimco obtained the material from Saf-T-Grip Specialties ("STG"), which in turn obtained the material from Alpha Extruders ("Alpha"). (Pet. App. 7a-8a, 21a).

The contract specifically required the Corps to test every 200 linear feet of waterstop to confirm that it met the specifications. (Pet. App. 6a-7a, 10-13a). Both parties understood that the Corps, and not Granite, was responsible for all testing of the waterstop, as evidenced by the Corps area engineer's memorandum stating that testing of the waterstop was the sole responsibility of the government. (Pet. App. 11a). The Corps tested one pre-delivery sample of the waterstop submitted by Granite. Granite later forwarded certifications provided by its second tier supplier, STG, stating that the waterstop shipped to the job would be from the same lot as the original samples. The Corps elected not to test every 200 linear feet of waterstop as the specification required but did not inform Granite of this decision. Granite assumed that the Corps had continued to test the waterstop before installation as required by the contract. (Pet. App. 8a-9a).

The Corps subsequently decided to test the waterstop after approximately 10% of it had been installed in the lock concrete. It found that the waterstop tested 13% below the tensile strength and ultimate elongation specifications. Based on the test results, the Corps directed Granite to remove and replace the

embedded waterstop. (Pet. App. 9a-10a, 13-16a). Granite requested that the Corps provide the design criteria and calculations for the waterstop so that Granite could hire a consultant to determine whether the embedded waterstop was adequate for its intended purpose. (Pet. App. 13a-14a). The government, however, refused to provide the design criteria, stating that it would consider nothing less than perfect compliance with the specified waterstop quality requirements. Without making any technical evaluation, the Corps directed that the waterstop be chipped out of the concrete and replaced. (Pet. App. 10a, 13a-16a).

Granite removed and replaced the waterstop as directed at extraordinary cost. In order to remove the waterstop, Granite had to chip the waterstop out of the concrete walls and replace it with new waterstop. (Pet. App. 14a-15a, 21a-22a, 81a). At trial, which was confined to the issue of liability, the government conceded that the cost of removing and replacing the waterstop exceeded $400,000. Granite presented evidence that the total cost resulting from removal and replacement of the waterstop was approximately $3.8 million. The original cost of the waterstop, fully installed, was $5,752.80. (Pet. App. 21a).

2. Granite pursued its claim before the Corps of Engineers Board of Contract Appeals on the bases that (1) the Corps failed to perform the required testing under the contract and was liable for the additional costs resulting therefrom, and (2) the Corps' demand to remove and replace the installed waterstop, without any technical evaluation, was improper because the waterstop was more than adequate for its intended purpose, and removal constituted economic waste. Five years after the trial, and without

participation of the trial judge, who had retired, the Board rejected Granite's claim. One judge dissented. (Pet. App. 3a-4a).

The Board majority found that the contract placed the primary responsibility for testing of the waterstop on the contractor. The Board majority further determined that the Corps had an absolute right to demand strict compliance with the contract and did not have to consider the adequacy of the embedded waterstop. (Pet. App. 3a-4a).

The dissent found that the Corps was liable for its failure to test in accordance with the contract provisions. The dissent also concluded that the Corps acted arbitrarily and capriciously in directing complete removal and replacement of the embedded waterstop without any technical evaluation, and was liable for the resulting cost. (Pet. App. 3a-4a; 101a-103a).

3. The United States Claims Court affirmed the Board's decision. It concluded that the contract gave the government the right to test but did not impose a duty to test. (Pet. App. 43a-44a). The court also found that the government, "like any other party to a contract, is entitled to receive that for which it contracted and had a right to accept only goods that conform to the specifications." (Pet. App. 46a). While the court recognized that there were limitations of reasonableness to the strict compliance doctrine, it rejected the concept of economic waste. (Pet. App. 47a-49a).

4. The Court of Appeals for the Federal Circuit determined that the government was solely responsible for testing the waterstop, and was therefore

liable "for performance delays attributable to an unreasonable failure to conduct periodic testing of the waterstop." (Pet. App. 12a). It found, however, that in light of the supplier's certifications it could not say that the Corps acted unreasonably in forgoing testing of the waterstop. It therefore concluded that the government should not be held accountable for its untimely testing. (Pet. App. 12a-13a).

On the economic waste issue, the court concluded that the only reasonable finding of fact that could be made on the record was that the embedded waterstop was adequate for its intended purpose. It noted that the margin of safety was twenty times greater than required for the project, and that it could withstand water pressure forty times greater than would ever occur. (Pet. App. 16a-18a). It noted that the government made no technical evaluation of the adequacy of the nonconforming waterstop and offered no testimony that it was not fully adequate. The court concluded that the Corps acted arbitrarily and capriciously in refusing even to consider any repair proposal that did not require total removal and replacement of the embedded waterstop. (Pet. App. 15a-16a). Accordingly the court found that the requirement to remove and replace the embedded waterstop constituted economic waste. (Pet. App. 21a-22a). It pointed out that the concept of economic waste had long been established at common law, had been applied by the federal boards of contract appeals in numerous cases involving government contracts, and had been cited by the Court of Claims. (Pet. App. 20a-21a).

The court also pointed out that under clause GP-10(b) of the contract, the contractor was required to

replace nonconforming material "unless in the public interest the government consents to accept such material or workmanship with an appropriate adjustment in the contract price." (Pet. App. 15a). As a result, it concluded that the government had the discretion to accept the nonconforming waterstop and "was required under GP-10 to consider the public interest when deciding whether to replace" the waterstop. (Pet. App. 15a). The court found that "the only real criterion used by the Corps in directing the removal and replacement of the waterstop was strict compliance with the specifications." (Pet. App. 16a). The Corps refused to consider whether it was in the best interest of the government to leave the waterstop in place and accept a credit. This, the court determined, was arbitrary and capricious. (Pet. App. 16a).

SUMMARY OF ARGUMENT

The United States Court of Appeals for the Federal Circuit exists in part to provide a single forum to hear appeals of government contract cases. In this case, in light of all the facts and its expertise in the law and realities of the government contracting process, that specialized court held that the contracting officer could not arbitrarily and capriciously require the contractor to tear out completed construction at extraordinary expense to replace $5,750 of material that exceeded petitioner's needs, because to do so amounted to economic waste.

The decision below does not warrant review by this Court. It poses neither a conflict in the lower courts nor a conflict with a decision of this Court. It does not raise an important question of federal law. Rather, this is a highly unusual case, involving both an ab-

solute failure by the contracting officer to exercise the discretion entrusted to him and extraordinary waste resulting from that failure. The Federal Circuit's application of the "economic waste" principle to the facts of the case is correct on the merits. The decision provides no opportunity for contractors to manipulate the bidding process, nor does it interfere with the government's use of uniform specifications. Moreover, petitioner has a prospective remedy that does not require the aid of this Court, *i.e.*, the unilateral power to prescribe an appropriate clause in future contracts.

ARGUMENT

A. Longstanding Principles of Federal Procurement Law Support the Federal Circuit's Application of the Economic Waste Doctrine

Contracting parties expect their partners to exercise contract rights in a manner that is reasonable and not arbitrary or capricious.[2] Accordingly, the courts and boards of contract appeals regularly resolve disputes with reference to mature federal common law "implied duties" or notions of "substantial performance", not spelled out in the contract, but founded in common sense and reasonable commercial expectations. Taken together these principles establish a set of generally-understood "ground rules" for the interpretation of contract terms. Because these ground rules exist to give effect to the parties' presumed intent, they apply equally whether the contract language is negotiated by the parties or mandated by regulations.

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[2] *Ripley v. United States*, 223 U.S. 695, 701-2 (1912); *Gadsden v. United States*, 78 F. Supp. 126, 128 (Ct. Cl. 1948).

No one disputes that the rule of strict compliance in the law governing construction contracts between private parties is tempered by an "economic waste" exception.[3] Respondent disagrees with petitioner's assertion that the decision below newly introduces the concept to government construction contracts. (Pet. 13-14). On the contrary, the principle of substantial performance, of which "economic waste" is a species, is well established in that law.[4] Moreover the rec-

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[3] *Jacob & Youngs, Inc. v. Kent*, 230 N.Y, 239, 129 N.E. 889 (1921); RESTATEMENT (SECOND) OF CONTRACTS §§ 241 and 348 comment c (1981); Annotation, *Modern Status of Rule as to Whether Cost of Correction or Difference in Value of Structures is Proper Measure of Damages for Breach of Construction Contract*, 41 A.L.R. 4th 131 (1985).

[4] In construction (as opposed to supply) contracts the principle is particularly vital and provides that in some circumstances substantial performance will be deemed equivalent to full performance. For example, the standard clauses entitled "COMMENCEMENT, PROSECUTION, AND COMPLETION OF WORK" (FAR 52.212-3) and "LIQUIDATED DAMAGES" (FAR 52.212-5) provide for liquidated damages to accrue if the contractor has not completed the work by the established completion date. The courts and boards have, however, interpreted these clauses to mean that liquidated damages will not accrue if the contractor's work is "substantially complete." *Continental Ill. Nat'l Bank and Trust Co. v. United States*, 101 F. Supp. 755 (Ct. Cl.), *cert. denied*, 343 U.S. 963 (1952). Similarly, courts and boards have generally held that an oral (or other "constructive") notice of intent to assert a claim under the "CHANGES" clause (FAR 52.243-1) is sufficient despite the clause's stated requirement of written notice. *See, Calfon Constr., Inc. v. United States*, 18 Cl. Ct. 426 (1989), *aff'd*, 923 F.2d 872 (Fed. Cir. 1990). The rationale is to avoid a forfeiture of an otherwise valid claim when the government has not been prejudiced by the lack of written notice. The principle also applies to the government's obligation to pay. The contractor may not abandon the work

ognition of an "economic waste" principle *per se* goes back at least twenty-six years and has been applied when the facts have been compelling enough to justify its use.

The relatively young Federal Circuit has not had occasion to consider the economic waste principle until this case, but its predecessor, the Court of Claims, confronted the issue in *H.L.C. & Assocs. Constr. Co. v. United States*, 367 F.2d 586 (Ct. Cl. 1966). Petitioner has mischaracterized the holding in *H.L.C.* in stating that "the Court of Claims [in *H.L.C.*] held that the doctrine of economic waste should not apply in government contract disputes." (Pet. 14). Instead, the court there denied relief because the facts did not support a finding of economic waste.[5] The fact that

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unless the government's default is "material." *See Northern Helex Co. v. United States*, 455 F.2d 546 (Ct. Cl. 1972), *on further proceedings*, 524 F.2d 707 (Ct. Cl. 1975), *cert. denied*, 429 U.S. 866 (1976), *on further proceedings*, 634 F.2d 557 (Ct. Cl. 1980).

[5] In *H.L.C.* the contractor sought to recover the cost of being directed to replace two-conductor wire, known to be nonconforming when installed, with three-conductor wire, arguing that they were equally suited to the government's needs. The Court of Claims described the "economic waste" doctrine and quoted from Judge Cardozo's opinion in *Jacob & Youngs v. Kent*, 230 N.Y. 239, 129 N.E. 889 (1921) The court held: "Our conclusion is that the requisite ingredients for the test of substantial performance—forfeiture and economic waste—are not present in this case, and that the doctrine of substantial performance is therefore inapposite." *H.L.C.*, 367 F.2d at 600. Petitioner's reliance on other cited Court of Claims decisions is also misplaced. *Farwell v. United States*, 148 F. Supp. 947, 949 (Cl. Ct. 1957) supports respondent's position. Farwell installed nonconforming but adequate copper tubing in part of a building. For the *installed* material, the government received a credit for only the

the court discussed economic waste without disapproving its application to government contracts can fairly be read not as a rejection of the principle but as an endorsement.

The economic waste exception has been recognized by the boards of contract appeals at least since 1974, when it was applied in *Valley Asphalt Corp.*, 74-2 B.C.A. (CCH) ¶ 10,680.[6] With the exception of the

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difference in cost between the conforming and nonconforming material, exactly the remedy respondent originally sought. With respect to the *uninstalled* material, the court held that the government had a right to demand strict compliance. *S.S. Silberblatt, Inc. v. United States*, 433 F.2d 1314 (Ct. Cl. 1970) did not involve an allegation of economic waste, but was based on a finding that the government's action in demanding removal and replacement was "manifestly reasonable under the circumstances." *Id.* 433 F.2d at 1323. In *Troupe Bros., Inc. v. United States*, 643 F.2d 719 (Ct. Cl. 1980) the contractor did not allege economic waste. It argued that the fact that there was no engineering justification for certain work supported his interpretation that the work was not part of the contract. *Id.* at 722-23.

[6] In *Arnold M. Diamond, Inc.*, 73-2 B.C.A. (CCH) ¶ 10,359, at 48,925, the board held that the government could not order replacement of nonconforming concrete at contractor's expense when repair would bring it into compliance. On the facts of *Eller Constr., Inc.*, 83-2 B.C.A. (CCH) ¶ 16,560, at 82,367-68, the board determined that removal of nonconforming concrete, rather than repair, was appropriate, citing *Valley Asphalt* and *Jacob and Youngs v. Kent. See also, Pacific W. Constr., Inc.*, 86-2 B.C.A. (CCH) ¶ 18,816, at 94,824 (board endorsed economic waste doctrine but denied relief on the facts); *Toombs & Co., Inc.*, 91-1 B.C.A. (CCH) ¶ 23,403, at 117,432-33 (board found in favor of contractor based on economic waste); and *Hunter Ditch Lining*, 91-2 B.C.A. (CCH) ¶ 23,673, at 118,565 (board cited economic waste analysis as appropriate but denied appeal based on contractor's failure to establish the fact of economic waste

Board and Claims Court in this case, no court or board has ever rejected the legal doctrine of economic waste in a government contract case.

The economic waste issue has come up infrequently in government contracts cases, but not for lack of precedent. Its infrequent appearance is rather because the doctrine operates in the realm of factual extremes (*e.g.*, demand to replace completed work despite high cost and without significant benefit) that simply do not arise often in practice.

B. The Federal Circuit's Application of the Economic Waste Doctrine is Consistent With the Terms of the Contract

The Federal Circuit did not derive the principle of economic waste from the "public interest" proviso in GP-10, as petitioner suggests. (Pet. 9, 16). Rather, the court determined that the common law doctrine of economic waste imposed an implied restraint on what it held to be "arbitrary and capricious" behavior by the contracting officer. (Pet. App. 16a).

This is not to say that GP-10(b) does not, by its own terms, require the contracting officer to consider economic waste in the "repair vs. replace" analysis. GP-10(b) provides:

> The contractor shall, without charge, replace any material or correct any workmanship found by the Government not to conform to the contract requirements, unless in the public interest the Government consents to ac-

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or suitability of the as-built project). *See also*, R. Bednar, H. Braude, J. Cibinic, Jr., G. Ginsburg, J. Margulies, R. Nash, Jr., D. Patin, and A. Stephenson, *Construction Contracting*, 804-10 (1st Ed. 1991).

> cept such material or workmanship with an appropriate adjustment in contract price. (Pet. App. 29a).

The first part of GP-10(b) gives the government the usual right to require correction or replacement of nonconforming work. The remainder of the clause provides that the government has the discretion, consistent with the public interest, to accept nonconforming work with a price reduction. The public interest is broad enough to include considerations of economic waste, as there can be no public interest in causing resources to be squandered or a contractor to suffer damage for no reason.

The parties agree that GP-10 gives the government the discretion to accept nonconforming work with an appropriate credit. (Pet. 17). Petitioner, however, argues that the right to exercise discretion necessarily implies a right to exercise that discretion arbitrarily, unless the contract language states otherwise. (Pet. 16-17). This argument reverses the common law presumption that contracting parties do not intend a grant of discretion to justify arbitrary behavior unless that intent is expressed clearly. When the contract entrusts discretion to the contracting officer, the officer has an implied duty to: 1) actually exercise that discretion, *Schlesinger v. United States*, 390 F.2d 702 (Ct. Cl. 1968), and 2) exercise that discretion in a way that is not arbitrary and capricious. *Hoel-Steffen Constr. Co. v. United States*, 684 F.2d 843 (Ct. Cl. 1982); *International Verbatim Reporters, Inc. v. United States*, 9 Cl. Ct. 710 (1986). Thus, regardless of whether the measure of discretion is "good faith," "substantial performance," "public interest," or "economic waste," the contracting officer breached his

duty in not exercising any discretion whatsoever. That default was an independent and sufficient basis for the court to have decided the liability issue in respondent's favor.[7]

In support of its argument that GP-10(b) gives it an unreviewable right to accept or reject nonconforming work, petitioner cites the "Value Engineering Incentive" clause (GP-66) of the contract and its current version, "Value Engineering-Construction" (FAR 52.248-3). (Pet. 13, n. 10). Under the value engineering clauses the contractor may suggest cost-saving specification changes and split the cost savings with the government if the proposal is accepted. Until the proposal is accepted, the contractor must proceed with the contract as written. The clauses do not address after-the-fact removal and replacement of nonconforming work.

The value engineering clauses reserve for the government the ultimate determination of what the contract specifications will say. Having provided the opportunity for contractors to offer value engineering suggestions, the government did not want to confront

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[7] The dissenting member of the Corps of Engineers Board of Contract Appeals panel would have decided the case in respondent's favor based, *inter alia*, on the contracting officer's failure to exercise any repair vs. replace discretion. (Pet. App. 103a). The court might also have cited, as the dissenting member of the board did (Pet. App. 102a), the implied duty of any contracting party to act reasonably and in good faith with respect to the exercise of its contract rights. This implied duty has gone by various names, including "implied duty to cooperate," *PBI Elec. Corp. v. United States*, 17 Cl. Ct. 128 (1989), and "implied duty not to hinder" performance, *George A. Fuller Co. v. United States*, 69 F. Supp. 409 (Ct. Cl. 1947); *Lewis-Nicholson, Inc. v. United States*, 550 F.2d 26 (Ct. Cl. 1977).

disputes over whether the rejection of a suggestion was or was not reasonable. Accordingly, the value engineering clauses, unlike GP-10, give contractors fair warning that the government's value engineering decisions are unreviewable. Subparagraph (e)(3) of the current clause provides in part:

> The contracting officer's decision to accept or reject all or part of any [Value Engineering Change Proposal] shall be final and not subject to the Disputes clause or otherwise subject to litigation under the Contract Disputes Act of 1978 (41 U.S.C. 601-613).

(App., *infra*, 1a-6a). If the government had wanted an unreviewable right to order removal and replacement of nonconforming work, regardless of economic waste considerations, it would have used the same language in GP-10.

In the twenty-six years since the *H.L.C.* decision, the government has had ample opportunity to modify GP-10 if it felt that the courts or boards were misconstruing the clause. The government has amended GP-10 since the Granite/Corps of Engineers contract was signed, but the language dealing with correction of nonconforming work was left alone. (Pet. 10-11, nn. 8, 9). The fact that the operative language has not been changed signals to the community of contractors that the government has been satisfied with such decisions as *H.L.C.*, *Valley Asphalt*, *Toombs*, and *Eller*.

C. No Provision of the Procurement Regulations Repudiates the Common Law Principle of Economic Waste

Petitioner makes the argument, not made at any prior stage of this case, that procurement regulations

bar a court from applying federal common law principles to "qualify" petitioner's assertedly unqualified right to demand strict compliance.[8] (Pet. 10, 15-16). Even assuming that the right were in fact unqualified by the wording of the clause itself, a contention that respondent disputes,[9] the argument is flawed in several respects.

Petitioner concedes that the federal courts have power to craft federal common law rules to govern government contracts. *See, Boyle v. United Technologies Corp.*, 487 U.S. 500, 504 (1988), *reh'g denied*, 489 U.S. 1047 (1989). No more in dispute is the principle that federal common law must give way to conflicting federal statutes, *City of Milwaukee v. Illinois*, 451 U.S. 304, 314 (1981), or valid regulations. This case does not test either principle.

Petitioner first reaches to elevate a definition of "specification" (48 C.F.R. § 10.001) to the status of a regulation in conflict with the federal common law doctrine of economic waste. (Pet. 16). In fact, the definition has no bearing on the economic waste doctrine. As a fuller text makes clear, the definition merely directs government contracting officers to avoid "gold-plating" when developing contract specifications: "Specifications shall state *only* the Government's actual minimum needs . . . ." (emphasis added).

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[8] The government's failure to raise this argument below has deprived this Court of the expert view of the Federal Circuit regarding the proper role of federal common law principles in interpreting mandatory clauses such as GP-10. Accordingly petitioner's argument should be deemed waived. *Singleton v. Wulff*, 428 U.S. 106, 120-21 (1976).

[9] Section B, *supra*.

Nothing in this definition purports to govern how a court should deal with completed work that in fact meets the government's minimum needs where its replacement would be economic waste.

Petitioner then argues that the language of GP-10, mandated by regulation, clearly conveys an intent that the contracting officer's discretion is unreviewable and that the Federal Circuit has thwarted that intent by "importing" a common law principle of economic waste. (Pet. 9, 16). The Federal Circuit decision was the result of an effort, not to thwart, but to effectuate the parties' presumed intent under the extreme circumstances presented in this case.[10] As a court with a deep understanding of both the principles and the practicalities of government contracting, the Federal Circuit was aware that GP-10 does not exist in a legal vacuum. Federal common law ground rules of contract interpretation were established long before this contract was signed and have persisted during the performance of many hundreds of subsequent contracts, all containing GP-10 in substantially the same

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[10] The Federal Circuit found that "the waterstop was entirely adequate for the project and that its replacement was unnecessary." (Pet. 22a). As Judge Cardozo observed in *Jacobs & Youngs v. Kent*, 230 N.Y. at 242; 129 N.E. at 891:

> From the conclusion that promises may not be treated as dependent to the extent of their uttermost minutiae without a sacrifice of justice, the progress is a short one to the conclusion that they may not be so treated without a *perversion of intention. Intention not otherwise revealed may be presumed to hold in contemplation the reasonable and probable. If something else is in view, it must not be left to implication.* There will be no assumption of a purpose to visit venial faults with oppressive retribution. (emphasis added)

form. If the government had wanted to change the ground rules it would have written GP-10 to convey that intent clearly. (Section B, *supra*). As the government did not do so, the court was right to assume that the parties intended that the implied duty to exercise discretion reasonably would continue to coexist in harmony with GP-10.

Although procurement regulations that mandate the use of standard clauses have been held to have the "force and effect of law,"[11] the courts have never treated such clauses as exempt from interpretation. To be sure, the wording of a mandatory clause is fixed by regulation, and the contracting officer is not authorized either to omit the clause[12] or to alter its wording.[13] The courts have never gone so far, however, as to hold that because a clause is mandatory, federal common law principles of interpretation are suspended. On the contrary, the courts regularly have interpreted such clauses in light of federal common law principles. See *Ronald A. Torncello and Soledad Enters., Inc. v. United States*, 681 F.2d 756, 770 (Ct. Cl. 1982) (mandatory termination for convenience clause qualified by common law concepts of consideration and mutuality); *Continential Ill. Nat'l Bank*,

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[11] *G.L. Christian & Assocs. v. United States*, 312 F.2d 418, 424 (Ct. Cl.), *reh'g denied*, 320 F.2d 345 (Ct. Cl.), *cert. denied*, 375 U.S. 954 (1963), 170 Ct. Cl. 902, *cert. denied*, 382 U.S. 821 (1965).

[12] *Id.*, 312 F.2d at 424.

[13] Any deviation from a mandatory clause which is made without the required authorization, *see*, FAR 1.403, is unenforceable. *McDonnell Douglas Corp. v. United States*, 670 F.2d 156 (Ct. Cl. 1982); *Southwest Marine, Inc., et al.*, 91-1 B.C.A. (CCH) ¶ 23,323.

101 F.Supp. at 757 (mandatory liquidated damages clause qualified by principle of substantial performance); and *Calfon Constr.*, 18 Cl. Ct. at 438-39 (mandatory changes clause notice provision qualified by principle of constructive notice).

D. The Federal Circuit's Decision Will Not Encourage Contractors to Base Their Bids on Nonconforming Products

Petitioner argues that if the economic waste exception is allowed to persist, any incentive for a rational contractor to bid on conforming components will "all but vanish," and the integrity of the public bidding system will be damaged. (Pet. 19). Petitioner's predictions are at odds with those practical realities of government contracting that the Federal Circuit was equipped to appreciate. They are also inconsistent with the fact that the "economic waste" principle applies only in extraordinary circumstances. The Federal Circuit's reiteration of the economic waste principle will have no effect on government contractor bidding practices, just as the Court of Claims' first articulation of the principle twenty-six years ago in *H.L.C.* has had no such effect.

The Federal Circuit decision does not alter or abolish the doctrine of "strict compliance" as it has existed for years in both private and government contracts. Nor does it grant the contractor a general right to insist on substituting nonconforming products, even if they may be superior to those specified. The government and private owner are almost always entitled to receive precisely what they specified. The economic waste principle applies only in those rare and extreme circumstances in which a reflexive application of the strict compliance rule would yield re-

sults that are so harsh compared to the benefits gained that they are presumed to be unintended.

No rational contractor would attempt to manipulate the procurement process to take advantage of the economic waste doctrine. To make its gamble seem worthwhile, the contractor would have to make a number of assumptions. In order to gain a competitive advantage the substitution would have to be of a major nonconforming component representing a substantial price differential. The more important the component, however, the more likely it is that the nonconformity would be detected. The contractor would have to assume that its employees participating in the bidding of the project would not discover and report the intended fraud. It would have to assume, further, that its workmen, foremen, superintendents and project managers at the site would not discover and report the nonconformity. The contractor would have to assume that its independent quality control representative[14] would either falsely certify that the work conformed to specifications or fail to discover the deviation. Finally, the contractor would have to assume that the government's full-time, on-site inspectors would fail to discover the nonconforming product. Each of these assumptions is problematic; cumulatively they are irrational.

The contractor will also face the reality that, if the nonconformity is detected, the greater the price dif-

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[14] On large construction projects the government generally requires that work be inspected and records maintained by a contractor quality control organization that is independent of the contractor's project management. *See, e.g., Santa Fe Engr's*, 81-1 B.C.A. (CCH) ¶ 14,976, at 74,102-03.

ferential, the more likely it is that the government will be able to articulate a quality-based rationale to reject the cheaper item. In all likelihood, if there is an equivalent major component that is less costly, the government will already have considered specifying it and will be able to state good reasons for not doing so.

If the government orders replacement, the contractor runs the risk that it will not prevail in any ensuing litigation. At that point the contractor is assured, at a minimum, of having to pay the difference in value between the as-built and as-specified structure. At the other extreme, the contractor risks the cost of replacement, almost certainly much higher than its original cost savings, plus the cost of litigating in a vain attempt to recoup its costs.

If these risks are not sufficient deterrents, the False Claims Act, 18 U.S.C. § 287 (criminal); 31 U.S.C. § 3729 (civil), and False Statements Act, 18 U.S.C. § 1001, provide the prospect of fines, imprisonment and debarment for contractors who invoice the government for material that they know to be nonconforming.[15] Any contractor who would not be deterred by these sanctions is unlikely to be deterred by the elimination of the economic waste principle.

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[15] *See United States v. Bornstein*, 361 F. Supp. 869 (D.N.J. 1973), *aff'd in part and rev'd in part*, 504 F.2d 368 (3rd Cir. 1974), *rev'd on other grounds*, 423 U.S. 303, *vacated without opinion*, 530 F.2d 964 (3rd Cir. 1976) (subcontractor held liable under 31 U.S.C. § 3729 for knowingly furnishing electron tubes not meeting specifications) and *United States v. Bass*, 472 F.2d 207 (8th Cir.), *cert. denied*, 412 U.S. 928 (1973) (subcontractor convicted under 18 U.S.C. § 1001 for fraudulently supplying deficient parts to the contractor and falsely representing that they were acceptable).

In the rare cases when the economic waste issue does arise, it will not be in the manner contemplated by petitioner, but in the manner reflected in this case. The waterstop was a $5,750 item on a $36 million contract. No competitive advantage was sought, or could have been gained, by bidding on waterstop that did not meet the specifications.

E. Adoption Of The Economic Waste Doctrine Will Not Encourage Litigation

No more persuasive is petitioner's argument that the Federal Circuit's application of the economic waste doctrine will encourage "pointless" litigation. (Pet. 19).[16] There is no reason to expect a flood of "economic waste" litigation in government contracting any more than in private contracting, which has not been thrown into disarray by the economic waste doctrine. In twenty-six years after the first discussion of the economic waste doctrine by the Court of Claims, there have been only a half dozen decisions involving that issue, despite the large volume of construction contracting financed by the federal government every year.[17] The paucity of such government construction

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[16] There are already sufficient deterrents to bringing "pointless" cases, *e.g.*, cost and the requirement that claims be certified pursuant to the Contract Disputes Act, 41 U.S.C. § 605(c)(1).

[17] Though large, the volume is not nearly as large as petitioner suggests. Petitioner cites Department of Transportation (DOT) construction expenditures of $1.3 trillion over the past five years. (Pet. 22, n. 16). Both the figure and the inference that petitioner draws from it are incorrect. According to the DOT Contract Information System, DOT spent only $1.86 billion in direct construction contracts in FY 1988-1992. Over the same period it spent $100.6 billion in the form of program grants for purposes including construction (*e.g.*, $24 billion under the Federal Aid

contract cases to date is the best indication that situations giving rise to an economic waste argument are extremely unusual. The reason is that in most cases, the contractor and government work together to find the least expensive method to provide the government with a product that meets its needs. Seldom does the government demand strict compliance when it results in economic waste.[18]

F. The Federal Circuit's Decision Will Not Discourage the Use of Uniform Specifications

Uniform specifications are generally written for the most severe conditions and therefore overstate the government's actual minimum needs with respect to most projects. Petitioner argues that an economic waste exception to strict compliance will undermine the use of uniform specifications by encouraging contractors to demand that a lesser product be substituted for the standard one. (Pet. 20-21). The doctrine

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Highway Program). These grants are not governed by the Federal Acquisition Regulation; the government is not a party to the resulting contracts; and the contracts are not required to include an "Inspection and Acceptance" clause such as GP-10.

[18] Petitioner argues that litigation of the economic waste doctrine will encourage "Monday-morning quarterbacking." (Pet. 10, n. 14). Using this case as an example, petitioner states that respondent's waterstop expert's opinion was developed for the Board and not presented to the Corps at the time the issue first arose. This assertion is misleading. When the problem first arose respondent requested that it be provided the design criteria for the waterstop so that it could retain an expert to review its adequacy. The contracting officer refused to provide the design criteria and was adamant in stating that he would accept nothing less than removal and replacement. In view of the government's position, respondent saw no point in retaining an expert at that time.

of strict compliance, however, prevents a contractor from simply "demanding" a substitution prior to installation. Strict compliance also applies after installation except in the unusual circumstance when economic waste would result. It is highly unlikely that the government will scrap its vast and useful system of uniform specifications simply because, in the very few cases when economic waste would result, it may not demand, at the contractor's expense, more than it needs. In the twenty-six years since *H.L.C.*, 367 F.2d 586, there is no suggestion that the government has curtailed its use of uniform specifications. The government will, and should, continue using uniform specifications unaffected by the decision in this case.

G. The Government Can Write the Economic Waste Exception Out of the Standard Contract Without the Aid of this Court

This Federal Circuit case does not involve a conflict with a decision of this Court or of any other court, nor does it involve statutory construction. *Cf. United States v. Goodyear Tire and Rubber Co.*, 493 U.S. 132 (1989), *reh'g denied*, 493 U.S. 1095 (1990) (Internal Revenue Code § 902); *United States v. American Bar Endowment*, 477 U.S. 105 (1986) (Internal Revenue Code §§ 511-13); *United States v. Hill*, *cert. granted*, 112 S. Ct. 1758 (1992) (Internal Revenue Code § 57(a)(8)). Here, petitioner has a remedy, revision of the standard form construction contract, wholly within its control.

The government can write the "economic waste" exception out of future contracts simply by amending clause GP-10(b) to state that the contracting officer's decision whether to require removal or replacement

is not reviewable under the Contract Disputes Act.[19] The government has previously rewritten standard clauses specifically to overcome the effect of Court of Claims decisions.[20] It has amended GP-10 before (to address matters unrelated to this case). (Pet. 10-11, nn. 8, 9). The government can do so again if it feels that it is good procurement policy to eliminate the principle of economic waste from federal construction contracting.

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[19] The government did just that in the case of the standard clause entitled "VALUE ENGINEERING-CONSTRUCTION" (Sec. B, *supra*). *See, DK's Precision Machining and Mfg.*, 90-2 BCA (CCH) ¶ 22,830 at 114,637.

[20] For example, the Default clauses, *see* FAR 52.249-8(d) and FAR 52.249-10(b)(1)(xi), were amended to provide that contractors are liable for the unexcusable delays of their subcontractors and suppliers at every tier after the Court of Claims held that a contractor was not liable for delays caused by a second-tier subcontractor in *Schweigert, Inc. v. United States*, 388 F.2d 697 (Ct. Cl. 1965). The same clauses were also amended to provide that a wrongful termination for default will be converted into a termination for convenience, thereby limiting recovery, after the Court of Claims held that a wrongfully-defaulted contractor could recover breach of contract damages in *Klein v. United States*, 285 F.2d 778 (Ct. Cl. 1961).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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December 1992